

Supreme Court of the United States.

OCTOBER TERM, 1897.

No. 158.

BUILDING AND LOAN ASSOCIATION OF DAKOTA,
Appellant,

v/s.

M. S. PRICE, ET AL.,

APPEAL FROM THE CIRCUIT COURT OF UNITED STATES FOR
THE NORTHERN DISTRICT OF TEXAS.

BRIEF OF APPELLANT.

STATEMENT OF THE CASE.

This suit was instituted by the appellant, a South Dakota corporation, against appellees, citizens of Texas, to foreclose a deed of trust and vendors lien executed in its behalf, on real estate in the city of Dallas, Texas, the bill of complaint alleging \$2800 and interest to be due on the lien. One of the defendants filed a demurrer to complainant's bill, challenging the jurisdiction of the court, on the ground that the matter in dispute did not exceed the sum or value of \$2000, exclusive of interest and costs. This demurrer was sustained and the suit was dismissed for want of jurisdiction of the subject matter. An appeal was prayed for and granted, the circuit judge certifying the question of jurisdiction to this court. In the original transaction out of which this suit arose,

appellant advanced the mortgagor the sum of \$2000. The only inquiry therefore, necessary to prosecute in order to determine the jurisdictional question involved, is whether such original transaction was solely one of borrowing and lending, and if so, whether either the \$2000 premium, or the excess of liquidated damages provided for in the bond, and which is sought to be recovered, is interest within the meaning of the jurisdictional statutes of United States, and if so whether a subsequent assumption of appellant's lien, by a vendee of the real estate involved, in the full sum of \$4000, created a vendors lien for such principal sum, so that the entire obligation was then to be treated as principal. Appellant prosecutes its appeal on the following

ASSIGNMENTS OF ERROR.

1. The bill shows that this court had jurisdiction of the subject matter in controversy.
2. The bill shows that the matter in dispute exceeds, exclusive of interest and costs, the sum of two thousand dollars (\$2000).
3. The bill shows that the controversy is between citizens of different states.

ARGUMENT.

I.

1. The bond secured by the deed of trust is on pp. 2 and 3 of the transcript. It is in the penal sum of \$4000, and recites that the mortgagor has bid in accordance with the by-laws of the appellant corporation the sum of \$2000 as and for a premium for the acknowledged advancement to him of \$2000, by way of anticipation of the value at their maturity of forty shares of the capital stock of said corporation, then owned by the mortgagor. It is conditioned that the mortgagor shall pay the appellant the sum of \$24 on the first day of each and every month thereafter, as and for the monthly dues on said shares of stock until the said stock becomes fully paid in and of the value of \$100 per share, and shall then surrender said stock to the appellant as security for the

faithful performance of the bond. It is also conditioned that the mortgagor will pay interest monthly at the rate of six per cent per annum on \$2000. It further provides in case of certain default, the existence of which is charged in the bill, the sum of \$4000 less whatever sum has been paid said association as and for the monthly dues on said forty shares of stock at the time of said default, may be enforced and recovered at once as liquidated damages, together with and in addition to the interest then due. The bill of complaint charges that the mortgagor accepted and received the said forty shares of stock according to the terms and conditions of a certificate issued by the appellant by which he agreed and promised to pay appellant on the first day of each and every month thereafter the sum of sixty cents for each and every share so held by him until such shares shall become fully matured and of the value of \$100 per share. (Transcript p. 2, ¶ 2.) The bill set forth that \$1200 for monthly dues has been paid. (Transcript, last ¶, p. 5.)

The original transaction was between a building and loan association and one of its members and share holders. The bond, therefore, contemplates a recovery for the failure to comply with the contract to make payments on the stock until it is worth \$100 per share. Mr. Endlich in his *Work on Building Associations*, (Second Edition) Section 124, says:

* * * * * "On the part of the borrower, this new contract may, in general, be said to embrace the following essential features: (1) The member agrees to receive the advancement from the building association, and to allow it, for the privilege of the preference, a certain stipulated price, premium, or bonus. (2) He undertakes, and gives security in support of his undertaking, faithfully to perform, to the termination of the society's existence, or the running of a series, all the requirements of its constitution and by-laws relative to stock payments or dues, fines and other charges upon and respect to the shares held by him (which, as a rule, he pledges to the society as collateral security), and to be liable for and discharge all proper dues, assessments, contributions, and charges, arising upon them, in the same proportion and in the same manner as the

rest of the members; and, in addition, to make a fixed periodical payment by way of interest on his loan, either by that name, or in the way of a stipulated increase in the regular dues corresponding with the interest upon the loan. (3) He agrees, that upon the termination of the society, when its assets shall become distributable, it shall appropriate the proportion thereof accruing to such of his shares as were advanced to him to its own reimbursement, and the payment of the premium bid, if the society runs its full course, or to its reimbursement merely if it be prematurely dissolved by reason of insolvency. (4) He agrees, that in case of his failure at any time to perform the continuing conditions of his undertaking, for a certain period; or for such remissness in the payment of dues, etc., as would be ground of forfeiture of his shares as a member, the society shall be absolved from the necessity of waiting, until the period of dissolution, for its payment, but shall have the right to demand and recover it from him at once, including in the debt, not only the amount actually loaned, but all the payments and charges which may, lawfully, under his obligation as member and borrower be demanded of him: And also in case of failure of the association and a winding up before its purposes are accomplished, to make settlement at once for what may be found due from him to it."

In the same work, Section 80, page 67, it is said:

"Remembering that the borrower is a member, and not the less so for being a borrower; that, consequently, his liability for his share of the expenses is complete during the continuance of his membership;—it is clear, that, had he remained a member he might eventually have set off a portion of the profit accruing to him from the common fund, against his proportion of the common expenses. By becoming a defaulter, he simply loses the right or expectancy, and gains nothing in the way of shaking off responsibilities already incurred. Now his mortgage, if as is usual, conditioned for the faithful performance of his membership duties, includes, beyond question, that of sharing in the expenses of the society, and may be used by it for the purpose of enforcing such contribution. If however, not so conditioned in express terms, its use for that purpose would, upon principle seem equally justified where the mortgage contract is based upon and refers to the contract of membership. 'The two things are so intertwined that you can not separate the contract of membership from the contract of mortgage.' The two therefore, forming

in truth but one contract, its view is, of course, to be gathered by a comprehensive view of the whole, and if the contract of membership, imported into that of the mortgage, embraces a liability to contribute to losses, the doctrine that the contract of mortgage can be satisfied without compliance with the contract of membership, in so far as the latter affects the value of the borrowers stock interest as an offset to his indebtedness, seems to be reduced to an absurdity."

The obligation, therefore, is not solely for the return of the money advanced, together with the promised premium, but it is also for the faithful performance of a stockholder's liability—to pay his agreed stock subscriptions. The fact that he has become a borrower does not release him from his agreement to pay these subscriptions, neither does it exonerate his stock from its liability to sustain its pro rata share of the losses, if any, of the corporation. The bond may possibly be said to contemplate a termination of the relation of stockholder upon the election of the corporation to enter suit after default, but if so, it further contemplates that with such termination the shareholder, in consideration of being released from the liability of having his being held for unpaid subscriptions and his stock impaired by reason of lawful charges incident to expenses, losses, etc., agrees to pay the corporation a certain amount as liquidated damages. This agreement insures him that he will receive from his stock the amount which has been advanced or loaned to him, and that the payments on his stock, no matter what its value, together with the promised liquidated damages will be received in full settlement of all his obligations to the corporation. Mr. Endlich, in Section 129 of the work already quoted from, says:

"The true view of this indebtedness, in fact, is that the return of the money received, at any period intermediate between the time of taking it and the time of ultimate squaring accounts upon the expiration of the society, or series, is not contemplated by the contract. The money is never before that period intended to be collected, or repaid. The essential feature of the contract is the continued payment of certain dues; the incident the payment of interest as a compensation for the

use of money. Even where the obligation is given for the repayment of a specific sum of money, with interest, the character it would seem to derive from the fact, is modified and overcome by the provisions which may follow as to the payment or dues, etc., showing clearly the true intent of the transaction, or indeed, from the fact that it was in truth a transaction between the society and its member. Such, then, being the real nature of the borrower's undertaking,—to stand by the society to its end, and to continue throughout, certain stipulated payments,—it would appear that the very terms of the contract precluded any determination of its requirements before the period set by itself. There are certain judicial utterances that would seem to indicate such as the view first held. But it promptly became recognized that a method by which the borrower would substantially comply with the requirements of his contract, might absolve him from the literal fulfillment of it; i. e., that, having obligated himself to a long series of small payments, he might be allowed to substitute, in lieu thereof, a single larger one, equal, at once, to the aggregate of the smaller ones."

The relation of the contracting parties is, therefore, such that they may contract as to the amount of liquidated damages, and the excess of such agreed amount of damages above the amount advanced is therefore not an accessory demand to be treated solely as interest agreed to be paid for the use of a money loan, but it becomes an element of the principal demand arising out of the complex relations of the parties. To hold that the excess of \$2000 is interest, would be to hold that appellant could not maintain an action in the Circuit Court seeking to recover on the original stock subscription, provided more than \$2000 was due thereon. Under the charges in the bill that an agreement exists to pay this subscription in the form of monthly dues appellant has the right, in case of a breach to sue for the balance due on the original subscription. (See *Endlich Id.*, Sec. 476.) Of course without an express agreement appellant could enforce payment for only these monthly dues actually in arrears, but by reason of the bond which authorizes suit to be maintained for the entire amount due, or for any specific sum as liquidated damages in lieu of the monthly payments, all sums, whether already due, or

to become due in the future, may be collected in one suit. This should be decisive of the question, and it is submitted that the judgment of the Circuit Court should be reversed and the cause remanded.

2. In the light of the following language in Section 130 of the work already quoted from, it may be doubted if, in the absence of any laws or rules governing the appellant corporation, the borrower, by the liquidated damage clause, can be deprived of an equitable right to make repayments,—either voluntary or involuntary—upon a basis far more favorable to him than provided in the bond. Mr. Endlich in the Section referred to says:

“The rule has been adopted in England, and recognized in America, that a borrowing member of a building association may redeem his property mortgaged, and discharge his indebtedness, to the same, upon payment of all future subscriptions which would accrue against him until the dissolution of the society, its probable duration to be ascertained by calculation, and the future payments to be treated as if immediately due.”

There is, however, nothing in complainants bill which, upon application of the foregoing rule, would indicate that an amount less than \$2000 is due on the stock. If the rule referred to were applicable in this suit, then its effect could be determined only after the defendants had answered and the probable duration of the series had been ascertained. The lack of jurisdiction by reason of the borrower claiming the right to apply the rule referred to could not, therefore, be determined upon demurrer.

3. But there are in this suit, rules and laws which govern the rights of the parties in case of repayment. The appellant pleads that it is a corporation duly and legally incorporated under and by virtue of the laws of the state of South Dakota. (Tr. p. 1.) The bond sued on purports to have been executed at Aberdeen, South Dakota, and recites that all payments thereon are to be made at appellant's home office in said city and state. (Transcript pp. 2 and 3.) The building and loan association laws in force in South Dakota in February, 1890, when the bond was executed, contain the following provisions:

“A borrower may repay his loan at any time by the

payment to the corporation of the principal sum borrowed, together with interest, not to exceed twelve per cent. per annum, * * * * * or (and) in case the amount of premium bid for the priority of such loan be deducted in advance, and the repayment thereof is made before the expiration of the eighth year after the organization of the corporation; there shall be refunded to such borrower one eighth of the premium paid for every year of the said eight years unexpired; provided, that when the stock is issued in separate series, the time shall be computed from the date of the issuing of the shares of stock on which the loan was made; provided further, that when the series of stock has a less period than eight years to complete full payment thereof, there shall be refunded only pro rata for the unexpired term of the series; and provided further, when the by-laws of the corporation prescribe a different manner, and terms upon which the loan may be repaid, then the repayment can only be made in accordance with the by-laws of such corporation. (Laws of Dakota, 1887, Chapter 34, Section 4, page 83.) (Session Laws, South Dakota, 1890, Chapter 105, page 254.)"

In the absence of any facts authorizing the application of any different rule permitted or prescribed by the above statute, the eight year clause thereof would govern, in case of voluntary repayment of the obligation involved in this suit. Mr. Endlich, in Section 140 of the work already quoted from, says:

"* * * Under such provision, if he repays, when the society is four years old, it having still four years to run, he is entitled to an allowance, in reduction of the debt, amounting to one half of the premium at which he took the loan. In computing this allowance, however, only whole years can be counted, and no claim can be made for proportionate allowances for additional fractions of years unless provision is made therefor."

The loan under consideration purports to have been made in February, 1890. (Tr. p. 2.) The stock is alleged to have been issued in January, the same year. (Tr. p. 1.) The bill of complaint was filed October 3, 1895. (Tr. p. 6.) The loan had therefore run nearly six full years, leaving two years premium to be rebated. This entitles the mortgagor to a rebate of one fourth of the original \$2000 premium, amounting to \$500, which leaves \$3500, from which deduct the \$1200 stock dues

shown to have been paid, and, under the above rule, in the absence of any right on the part of the borrower to any part of the accrued profits on his stock, there still remains due and unpaid the sum of \$2200 exclusive of interest. Conceding that the mortgagor is in position to invoke this statute to determine the amount due on his bond and it is clear that the amount in dispute is in excess of \$2000, exclusive of interest and costs. It is, however, held in *People's Ass'n vs. Belling* (Mich.) 62 N. W., 375, and in *Mutual Ass'n vs. Tascott*, (Ill.) 32 N. E. 377, that under statutes similar to the one quoted, the mortgagor, when sued on his obligation, can not avail himself of the rights accorded him in case of voluntary repayment. The application of the rule promulgated in these cases, is not, however, necessary to the determination of the question presented in the case under consideration.

4. In determining this question it is not necessary to discuss the law of usury as applicable to this class of contracts. An examination, however of the authorities touching usury may throw some further light on the character of the contract, and assist in determining whether the "premium" is interest. The term "usury" necessarily includes the term "interest." The same reasoning therefore, which determines whether building and loan association contracts in general are usurious, might determine whether the premium is interest. The laws of South Dakota. (Laws of Dakota. 1885, Chapter 34, Section 6, page 58), provide as follows:

"No premiums, fines, or interest on such premiums that may accrue to said corporation (Building and Loan Associations) according to the provisions of this act shall be deemed usurious; and the same may be collected as debts of like amount are now by law collected in this Territory."

Said laws (Session Laws of Dakota, 1889, Chapter 41, Section 3, pp. 60, 61) also provide:

"As building and loan corporations are aggregations of laborers, mechanics, workmen, and working women, which start without any paid up capital, and as these members only pay each month an assessment in proportion to shares, for the purpose of furnishing a home to

each of its members in turn, which assessment stops the moment that every member has thus been furnished with such home, these associations are declared to be benevolent institutions within the meaning of (certain laws exempting certain institutions from taxation) * * * *

* * Shares issued by such association shall be exempt from taxation."

The Dakota laws herein referred to have never been construed by the Supreme Court of the State of South Dakota. The same laws, however, became part of the law of the State of North Dakota on the division of Dakota Territory and the admission of the two Dakotas into the Union. The Supreme Court of the State of North Dakota, in *Vermont Loan & Trust Co. vs. Whitshed*, 49 S. W., 318, in considering these laws said:

"Under our statute the member has the right to pay his note at any time, and thus stop the interest, and in that case, would of course be entitled, on the dissolution of the corporation to receive the value of his stock in cash. But the effect of the transaction, generally speaking, is simply this: The association uses the fund to purchase the stock of that member who is willing to sell his stock in advance for the least money, and continue the payments on stock subscriptions until the value of the stock reaches par. It will be noticed that all the stock receives the benefit of the premiums paid, that of the party receiving the so-called loan, equally with that of the other stockholders, and the larger the aggregate premium the sooner the value of the stock will reach par, and the sooner the stated payments of stock subscription will cease. * * * It seems very clear to us that the operations of building and loan associations, when confined to their own members, differ so radically from ordinary loan transactions that the legislature was clearly warranted in placing such associations in a separate class for the purpose of such legislation as pertains to interest and usury; and the classification being once established, the extent to which the classes shall be separated is purely a matter of legislative discretion. The legislature has the right to leave such associations untrammelled in the matter of premium paid for loans, and it has an equal right to leave them untrammelled in the matter of interest proper."

In the case of *Richard vs Southwestern Assn. (La.)* 21 Southern, 643, the contract involved was identical with the one before this court. In its opinion therein, the court says:

"A mere loan of \$2000 would not be linked with a transfer of forty shares of stock to the borrower, imposing the burden on him of payment as well as entitling him to the benefits of a shareholder. * * * The plaintiff received the \$2000; has had the benefit of it at 6 per cent. along with the rights conferred on him as a shareholder."

In a recent South Carolina case, *Equitable Ass'n vs. Vance*, 27 S. E., 276, in which the contract was similar to the one at bar, the Supreme Court of that State says:

"The circuit judge might have gone further, and held that even under the laws of this state, the contract was not usurious. Referring to the rate of interest charged, he says in the decree: 'It is not more than six per cent., because \$7.50 per month is exactly six per cent. of \$1500. The other payments are independent of the loan and had to be made whether a loan was made or not.' Here he touched the very marrow of the matter, when he indicated that the payments made by the defendant referred to two distinct transactions, which should not be blended."

II.

There is such a substantial difference between the "premium" of this transaction, and interest in the ordinary acceptance of the latter term, that it seems unnecessary to resort to any technical definitions to show that this "premium" is not interest. It is, however, submitted that the term "premium" in building and loan association law has a meaning which is as technical as the same term applied to either the law of insurance or to the value of stocks and bonds. Mr. Endlich, in Sections 399 and 400 of the work already so freely quoted from, says:

"The premium is a bonus charged to a stockholder wishing to borrow, for the privilege of anticipating the ultimate value of his stock, by obtaining the immediate use of the money his stock will be worth at the winding up.' The liquidation of this charge is contemplated in one of two ways. Either (1) the borrower agrees to relinquish to the society a certain proportion of the par value of each share bought out, the association presently handing over to him the difference. * * * * The former method is the gross premium plan, the orig-

inal and interminating and serial societies probably the prevailing one."

"In effect the gross premium is the conventional difference between the par value of the share advanced, and the amount actually received by the borrower. It is not, therefore, a cash payment which he is obliged to make upon obtaining his preference; nor can it properly be said to be a deduction made at the time from any money belonging to him. Its true nature appears most clearly where the form of the transaction is that of a sale to, and redemption by, the society of the shares held by the member, which indeed, appears to be the oldest method."

The bond in the suit at bar recited (Tr. p. 3.):

"Whereas, said Jacob Rothchild has bid, in accordance with the by-laws of said association, the sum of \$2000 as and for a premium for the advancement to him by said association of \$2000 by way of anticipation of the value at their maturity of the the forty shares of the capital stock, etc."

The bill charges (Tr. p. 2) that the mortgagor made application for said advancement in anticipation of the maturity value of said shares, and that in competition with other bidders for the funds of appellant he bid as a premium for the privilege of obtaining such advancement the sum of \$50 per share. The laws of South Dakota, (Laws of Dakota, 1887, Chapter 34, Section 3, page 82,) define the term premium in the following provision:

"The officers shall hold stated meetings at which the money in the treasury shall be offered for loan in open meeting and the stockholder who shall bid the highest premium for the preference or priority of loan shall be entitled to receive a loan for the full amount of each share of stock held by such stockholder."

Interest is compensation paid, or agreed to be paid for the loan, use or forbearance of money.

Premium in building and loan association law is the discount which the borrower makes on his shares for the privilege of realizing on them immediately.

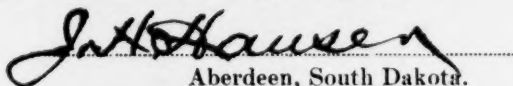
III.

The bill of complaint charges that the original mortgagor conveyed the mortgaged premises to the defendant Sophia Miller, who, as a part of the purchase price

therefor, assumed and agreed to pay the aforesaid bond, in the sum of \$4000, secured by the aforesaid deed of trust lien, retaining a vendors lien in the said deed of conveyance to secure the payment of the said sum of \$4000." (Tr. p. 5, Original p. 9.)

In Texas a vendor's lien is recognized and is enforceable, and when retained by a vendor who is also a mortgagor, it inures to the benefit of the mortgagee. Texas Land & Loan Co. vs. Watkins, 34 S. W., 996. The assumption as pleaded therefore gave the vendor, who was the original mortgagor, a lien in the principal sum of \$4000, and the vendee is, by such assumption estopped from denying the validity or existence of the mortgage or that there is \$4000 due thereon. (Jones on mortgages, Fifth Edition, Section 744.)

It is therefore respectfully submitted that the judgment of the Circuit Court should be reversed and the suit remanded for further proceedings therein.


Aberdeen, South Dakota.


Dallas, Texas.

Attorneys for Appellant Building & Loan Association of
Dakota.